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C O N F I D E N T I A L SECTION 01 OF 03 QUITO 002578

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SUBJECT: PROCURADOR'S INVOLVEMENT IN OXY AND OTHER MATTERS

REF: QUITO 2236

Classified By: EconCouns Larry L. Memmott, Reasons 1.4 (b&d)

1. (C) Summary: At Occidental Petroleum's (Oxy) and the GOE's request, EconOffs met with Ecuador Solicitor General (Procurador General) Jose Maria Borja November 7, to lay the groundwork for Borja's buy-in to the ongoing discussions between Oxy and members of the GOE. Recently, Oxy has had its most serious discussions to date with members of the GOE regarding a resolution to its commercial disputes with the GOE. The involvement of the Procurador, who actually created the problem, is not welcome by anyone, but is unavoidable. The fact that the GOE thinks it's time to bring Borja into the talks could be construed as progress. However, Borja cannot be trusted and his involvement will complicate matters. In the end, pressure from a variety of sources will be needed to get Borja to do the right thing, as his interpretation of the law depends upon how he is feeling at any particular moment. End Summary.

Bring in Jose Maria and Hold On to Your Wallets

2. (C) Oxy has held secret discussions over the last two months with the President of PetroEcuador Luis Roman and President Palacio's advisor and now Ambassador to the United Nations Diego Cordovez. In a refreshing change for Oxy, Roman actually knows the oil sector very well. While the GOE has still not responded with its own counteroffer to Oxy's various offers, the two sides have developed a good working relationship and some progress had been made toward a resolution. At Palacio's express instruction, knowledge of the discussions was kept strictly to Oxy, Palacio, Roman, Cordovez, and us. When Minister of Energy Ivan Rodriguez threatened to resign (reftel) he too was informed of the discussions, but had not participated in them.

3. (C) Oxy called Econoff November 4 to request that Embassy officials approach Procurador General (similar to the U.S. Solicitor General) Jose Maria Borja. Roman had called Oxy and said the GOE needed to get Borja on board in the negotiations and wanted the Embassy to approach Borja first to lay the groundwork for Roman and Rodriguez to meet with him.

4. (C) Econoffs met with Borja on November 7 to deliver the message. Borja first regaled Econoffs with his efforts to insert himself into any area where there was a vacuum in the government. For instance, he claimed that he was "taking over" the two state phone companies. The following day, the newspapers reported changes in the directors of both Pacifictel and Andinatel. Borja said he also intended to insert himself into the electric sector and we heard through other sources that he had tried to negotiate a gas deal with Venezuela.

5. (C) Borja then offered a "resolution" to the multi-billion dollar Chevron lawsuit (reftel) pending in Ecuador (with other legal processes in the United States). His resolution - Chevron need only place \$500 million into a trust fund for environmental remediation and the GOE would put up the same amount. As to Chevron's remediation agreement that releases the company from further liability, Borja responded that it was agreed to by corrupt former Ecuadorian officials and therefore was not binding. He did not explain why the GOE has not prosecuted these allegedly corrupt officials. Econ Counselor responded that Chevron believed it had a strong case and that it would ultimately prevail in court.

6. (C) Taking advantage of Borja's hubris, Econ Counselor asked the Procurador about the sale of Canadian oil company EnCana's Ecuadorian assets to a Chinese consortium. That sale is contingent on resolution of the Oxy caducity issue. A smiling Borja told Econoffs that the Chinese had been in to see him on the matter. He said that he told the Chinese that they had just bought themselves a lottery ticket!

7. (C) Apparently delighted that he was now being asked by us to become involved in the Oxy discussions, Borja was quick to offer his views to Econoffs. First, the state/company share of revenues would have to be changed. Incorrectly stating the Oxy received 72% of the oil revenues to the GOE's 38% share, Borja said the split should be 60/40, in favor of Oxy

and should be backdated to 2000, when the Block 15 transaction between Oxy and EnCana began. (Note: when royalty, tax and other payments are taken into account, the state share is already over 60%.) Second, Oxy would have to accept the declaration of caducity (contract nullification, which under Ecuadorian law would mean that Oxy's assets in Ecuador would devolve to state-oil-company PetroEcuador, without compensation to Oxy). However, Borja said that we should not worry because immediately after the declaration of caducity, the GOE could announce the new contract the GOE negotiated with Oxy to resolve Oxy's violation of the law. Econ Counselor pointed out that if caducity was declared it seemed that under Ecuadorian law a bid solicitation process might be needed, as Oxy's assets would have devolved to PetroEcuador as a result of the caducity declaration. Borja dismissed that as unnecessary.

18. (C) Borja's other brilliant idea was to have the President of Oxy in the United States come to Quito to sit with Borja and President Palacio and the three of them would negotiate a resolution, including the terms of the new contract. Borja backed away from that proposal when Econ Counselor noted the complexity of such negotiations and the need for technical discussions prior to presenting any agreement to Palacio. Still, he said, at some point Palacio, the President of Oxy and he would need to get together to agree on the final resolution. Moments later, however, Borja contradicted himself and said that neither he, nor his office would be involved in the negotiations, other than to approve their outcome.

19. (C) The night of November 7, Borja called Econoff at home to discuss a new procedure for settling the Oxy case. Borja said that Minister of Energy Rodriguez, PetroEcuador President Roman and he had met that evening with President Palacio. Borja announced that a commission had been formed to resolve the Oxy matter. He would only give one of the names of the commission members to Econoff, Borja's designate Pedro Freile. The other commission members would be one representative each from the Ministry of Energy, PetroEcuador and SRI (the Ecuadorian Internal Revenue Service). The commission, according to Borja, is supposed to come up with a counteroffer by Sunday, November 13 to present to Oxy (whom he said should also name a commission, but did not explain why). The two "commissions" would then agree on the final resolution. Once that resolution was reached, the commissions would "disappear." Minister of Energy Rodriguez would then appoint his own well-respected expert, who would recommend the same solution reached by the "disappeared" commissions, whom no one would know about. Rodriguez would next present the proposal of the secret commissions to President Palacio for approval. According to Borja, the entire process should only take 45 days.
Borja Playing Fast and Loose with the Truth

110. (C) In his November 7 meeting with Palacio, Roman and Rodriguez, Borja told them that the U.S. Embassy agreed that Oxy would admit fault and thus accept caducity. Roman and Rodriguez called Oxy to ask if this were true and Rodriguez contacted the Embassy to question Borja's assertions. Econ Counselor and Senior Commercial Officer met with Minister Rodriguez November 8 to assure him that nothing of the sort was stated by EconOffs in their meeting with Borja the day before. Oxy gave Roman and Rodriguez the same message.

Oxy's Reaction -----

111. (C) Oxy met with Roman and Rodriguez November 8 where the idea of a commission was discussed. They agreed that they would move forward on their own with the talks between Oxy, Roman and Cordovez (and not wait for the commission to come up with any numbers). The next meeting would be November 11 and Roman provided Oxy with some "general" numbers, the closest that Oxy has seen to a counteroffer from the GOE. At their next meeting, the parties would try to reach an agreed amount that could be presented to the new commission the following week.

112. (C) The most positive developments to come out of this week's events is the affirmation by Minister Rodriguez that he would resign rather than declare caducity against Oxy. Rodriguez and Roman also believed that they were successful in convincing Borja that a declaration of caducity was not possible if the GOE wanted to negotiate a settlement with Oxy. Roman told Oxy that he believed that Borja was "all show" and that President Palacio is now convinced that Borja is a liar because of his untrue allegations of the Embassy's position regarding Oxy's alleged acceptance of a caducity declaration.

Herreria: Palacio Wants to Decide for Oxy -----

113. (C) In a separate meeting, Presidential advisor Luis

Herreria told Pol Counselor that President Palacio wants to decide in favor of Oxy on the caducity issue. Herreria said that the U.S. Embassy should start laying the groundwork with the press to sway public opinion in favor of a negotiated solution that would keep Oxy in the country. Pol Counselor asked Herreria if the GOE would also be working to create such an environment. Herreria responded with an unconvincing yes.

Comment

14. (C) We have kept the Procurador at arms length, particularly in the last two months when it appeared that discussions between Oxy and the GOE might finally start to show signs of progress. It was inevitable that Borja had to be brought back into the process. The fact that the GOE asked us to help bring him back in now is some indication that the GOE feels it is coming closer to being able to reach a settlement with Oxy. As we expected, Borja will be more of a hindrance than help. Still, the fact that the major participants in the process recognize Borja's true nature will help to limit his influence. Besides, this is the first time that the Ministry of Energy, PetroEcuador, the Presidency, the Procurador and Oxy all seem to be working at the same time toward a common goal, a negotiated settlement with Oxy.

15. (C) However, with Borja's dishonesty and delusions of grandeur, and a general lack of GOE will to resolve any difficult problem, reaching a negotiated settlement in the near future is by no means assured.

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